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In The
SUPREME COURT OF THE UNITED STATES

No. 416

L. E. RIFFE, *Petitioner*,

vs.

WILSHIRE OIL COMPANY OF TEXAS, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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vs.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

L. E. Riffe respectfully petitions the Supreme Court of the United States for a writ of certiorari for review of the judgment of the United States Court of Appeals for the Tenth Circuit rendered in the case of Wilshire Oil Company of Texas, Appellant, versus L. E. Riffe, Appellee, on the appeal of a judgment entered by the United States District Court for the Northern District of Oklahoma, and, for such petition, states to the Court as follows:

I

REPORTS OF OPINIONS OF COURTS BELOW

The opinion of the United States Court of Appeals for the Tenth Circuit of which review is sought is reported at 406 F. 2d 1061. The opinion of that Court on a prior appeal in this case is reported at 381 F. 2d 646. Petitioner sought a petition for writ of certiorari for review of the prior opin-

ion, but his petition was denied by memorandum order of this Court which is reported at 389 U. S. 822, 88 Sup. Ct. 50. A copy of each opinion of the Circuit Court is appended.

The judgments rendered by the trial court, the United States District Court for the Northern District of Oklahoma, have not been reported, officially or unofficially.

II

GROUNDS ON WHICH JURISDICTION IS INVOLKED

The judgment of the United States Court of Appeals for the Tenth Circuit sought to be reviewed was entered on February 4, 1969, in accordance with the Court's opinion filed on the same date.

Petitioner applied for an extension of time from February 24, 1969, until March 3, 1969, in which to file a petition for rehearing. Such petition was filed on February 27, 1969, and denied by the Circuit Court on March 17, 1969.

On March 28, 1969, Respondent filed with the Circuit Court a pleading styled "Motion for Clarification of Mandate", to which Petitioner responded on April 3, 1969. The Circuit Court treated the "motion" as a petition for rehearing and denied it on May 29, 1969.

The statutory provision believed to confer on the Supreme Court jurisdiction to review the judgment in question on writ of certiorari is 28 U. S. C. §1254(1).

III

QUESTION PRESENTED FOR REVIEW

Petitioner, who was a director and salaried officer of

Respondent corporation, became aware of a business opportunity which he fully disclosed to the corporation. Respondent, acting through its board of directors, elected to seize and take advantage of the opportunity, but later reversed its decision and directed Petitioner to obtain the release of Respondent from all contractual obligations it had incurred with respect to the opportunity. Petitioner succeeded in obtaining Respondent's release. Third parties then formed a corporation to exploit the opportunity. One of such parties made a gift of stock in the newly-formed corporation to trusts for the benefit of Petitioner's children. Petitioner had no involvement with that corporation and continued to serve Respondent faithfully and well. He has already paid to Respondent an amount equal to the profit realized by the trusts from the stock. Is Petitioner also required to forfeit to Respondent all compensation earned during the period of ownership of the stock by the trusts?

IV

CONSTITUTIONAL OR OTHER ENACTMENT OF LAW INVOLVED

This case involves no constitutional provisions, treaties, statutes, ordinances or regulations.

V

STATEMENT OF THE CASE

On December 30, 1960, Respondent, by merger, acquired Riffe Petroleum Company, a closely-held corporation owned principally by Petitioner, which engaged in the marketing of asphalt and asphaltic materials. Subsequent to the merger, Riffe Petroleum Company continued substantially the same operations as a division of Respondent. Petitioner became executive vice president and a director of Respondent, his

primary responsibility being the management of the Riffe Petroleum Company Division.

In late 1961, Petitioner became aware of an opportunity to construct and operate an asphalt manufacturing plant at Ponca City, Oklahoma. This plant would be constructed on land of Cities Service Petroleum Company and operated in conjunction with its refinery, utilizing refinery by-products in the manufacture of asphalt. Petitioner negotiated a contract with Cities Service on behalf of Respondent for construction and operation of the asphalt plant and the supply of raw materials. This contract was approved and ratified by Respondent's board of directors and Petitioner proceeded with arrangements for construction.

Thereafter, Respondent changed its mind about owning and operating the plant and instructed Petitioner to extricate it from the contractual obligations that it had incurred. In order for him to accomplish that task, it was necessary for him to convince personal acquaintances of the attractiveness and soundness of the opportunity. These acquaintances then formed a corporation, Redstone Asphalt and Petroleum Company ("Redstone"), to construct and operate the asphalt plant. Redstone thereafter negotiated and entered into a contract with Cities Service for construction and operation of the asphalt plant, which contract was substantially identical to the earlier contract between Respondent and Cities Service. As a condition to releasing Respondent from its contract, however, Cities Service required that Petitioner personally guarantee performance by Redstone of its contract. Petitioner then made this guaranty in order to obtain the release of Respondent. Further, for Redstone to obtain the money needed to construct the plant, it was necessary for Petitioner to guarantee payment, to the extent

of eighty per cent, of a loan in the amount of $274,000.00, which Redstone obtained from a Tulsa bank. Respondent was fully informed of these guarantees by Petitioner.

A. V. Murray, originally a defendant in this case, one of Petitioner's acquaintances who had formed the Redstone corporation, owned sixty per cent of the capital stock of the corporation. While the asphalt plant was in the process of construction, Mr. Murray sought to sell to Petitioner at his cost one-half of that stock and to give to Petitioner one-half of a commission he was to receive from the company building the plant, in appreciation of Petitioner's having brought the opportunity to his attention initially. Petitioner declined the gratuity.

Subsequently, Mr. Murray arranged for the transfer of the stock and commission to the trustees of irrevocable trusts which Petitioner and his wife had previously created for each of their six daughters. As found by the trial court, Petitioner had no control or direction over these trusts, directly or indirectly, and had no interest therein, other than as settlor and a normal paternal interest. The transfers to the trust were not pursuant to any agreement between Mr. Murray and Petitioner.

In September, 1962, the asphalt plant was completed and commenced production. In December of that year, all of the stock of Redstone was sold to Inland, Inc., for approximately $112,000.00. For the thirty per cent of the stock owned by the trusts, $36,888.59 was received, resulting in a profit of approximately $28,000.00.

Respondent operated the Riffe Petroleum Company Division for a twenty-nine-month period and realized profits

of approximately $400,000.00 before selling the division to another firm at an additional profit of $377,000.00. Thereafter, in December, 1963, Respondent instituted this action, seeking, *inter alia*, to recover the profit made by the trusts on the sale of the Redstone stock and all compensation paid to Petitioner on the grounds that ownership of the stock by the trusts and other alleged misconduct on the part of Petitioner constituted breaches of his employment contract and fiduciary obligations to Respondent. Non-jury trial resulted in judgment for Petitioner and all other defendants on all of Respondent's claims, except one small claim, as to which the defendants confessed judgment. On appeal, the Circuit Court found that the transactions involving the asphalt plant and the stock of Redstone Asphalt and Petroleum Company constituted breaches of Petitioner's contractual and fiduciary duties to Respondent and remanded the case for determination of damages.

Upon remand, the District Court, following a hearing, found that the trusts had received a total of $35,913.59 in profit on the Redstone stock and the construction commission. Judgment for that amount, plus interest of $11,037.14, was rendered in favor of Respondent and paid by Petitioner.

Respondent, contending that the District Court had erred in not adjudging that Petitioner should also repay all compensation that he had earned during the period in which the Redstone stock was owned by the trusts, perfected the second appeal in this case. The Circuit Court held that its previous findings of a breach by Petitioner of his contractual and fiduciary duties to Respondent required that he forfeit and return to Respondent all of his earnings during that period.

VI

BASIS FOR FEDERAL JURISDICTION IN COURT OF FIRST INSTANCE

Jurisdiction of this case in the United States District Court for the Northern District of Oklahoma was founded on diversity of citizenship and amount. Respondent is a corporation incorporated under the laws of the State of Delaware, having its principal place of business in Colorado. Petitioner and the other defendants in the trial court are all citizens and residents of the State of Oklahoma. The amount in controversy exceeds $10,000.00, exclusive of interest and costs.

VII

ARGUMENT FOR ALLOWANCE OF WRIT

There is presently no area of civil law attracting greater concern and attention than that relating to the potential liability of corporate directors and officers. More articles in law reviews and commentaries, more time in seminars and institutes and more study by corporate counsel and other members of the bar have recently been devoted to this area than to any other aspect of the law, except possibly civil rights and criminal matters. While much of this interest has been sparked by *Escott v. Barchris Construction Company*, 283 F. Supp. 643 (S.D. N.Y., 1968), and *Securities and Exchange Commission v. Texas Gulf Sulphur Co.*, 258 F. Supp. 262 (S.D. N.Y., 1966), mod. and aff'd. 401 F.2d 833 (2nd Cir., 1968), and their progeny which involve the responsibilities of corporate "insiders" under the Securities Exchange Act of 1934, as amended (15 U.S.C. §78a *et seq.*), the concern is not limited to potential liability under that Act.

It is essential that, in the complex system of modern

commerce and industry, the managers of corporate enterprises be able to assess and determine reliably their obligations to the companies and stockholders which they serve, their freedom to engage in outside activities, and their economic liability to others if they overstep the ascertaintions imposed by law upon their activities, neglect, stagnation and failure to develop the myriad of business opportunities which are constantly presented will necessarily result.

In the situation presented by the facts in this case, under the law as theretofore developed, Petitioner would have been free to seize and exploit personally the opportunity presented. The Circuit Court changed the law, however, and applied unwarranted penalties. When the opportunity to own, operate and exploit the asphalt plant at Ponca City arose, Petitioner knew that it was potentially profitable to his employer, Respondent, to whom he owed duties of disclosure. Petitioner fully revealed the opportunity and urged Respondent to grasp the opportunity. Upon disclosure, Respondent said "yes" and Petitioner consummated the necessary contracts. Whatever the reason, Respondent changed its corporate mind and, acting through its board of directors, told Plaintiff to extricate it from its obligations to construct and operate the proposed asphalt manufacturing plant. At that point, the issue in this case, and the question presented by this petition was posed.

Having fully and honestly presented a business or corporate opportunity to the corporation which employed him as an officer and director and having had that opportunity rejected by the corporation, what was Petitioner's position with respect to personal exploitation?

(For the purposes of this petition, ignored are the legal implications of the fact that Petitioner did not thereafter have any personal involvement with the opportunity and that his sole, but indirect, connection therewith was the ownership by irrevocable trusts, of which his daughters were the beneficiaries, of stock of the corporation created by unrelated parties to exploit the opportunity.)

From the statement of the case, it is apparent that, had Petitioner done nothing after Respondent rejected the opportunity, Respondent would have faced substantial liability for breach of its contract with Cities Service and no one, investor or the public, would have benefited from construction and operation of the asphalt manufacturing plant. Such losses to all concerned are the inevitable consequences of the rule for which Respondent contends and which the Circuit Court has sanctioned and promulgated for those corporations, stockholders and fiduciaries within its geographic sphere. Petitioner submits that such a rule is contrary to established principles of law and equity and will have the unwarranted effect of restricting the development of commerce and industry.

The concepts of law to be analyzed in determining the right of an officer or director of a corporation to avail himself of an opportunity rejected by his corporation are a curious amalgam of the principles historically applicable to the relationships of masters and servants, agents and principals and trustees and beneficiaries. This lack of clear definition of applicable principles was exemplified in *Lydia E. Pinkham Medecine Co. v. Gove*, 303 Mass. 1, 20 N.E. 2d 482 (1939), wherein the court drew upon various unrelated concepts to assess the rights of a corporate employee.

In its decision in this case, the Circuit Court has established the rule that a corporate fiduciary, who acquires an interest in a venture which his corporation has rejected, must not only lose any profit obtained, but must, additionally, bear the harsh penalty of forfeiture to his employer of any compensation earned for his faithful service during the period of ownership of an interest in the rejected venture. This rule is invoked and applied without regard to the gain realized by the corporation during the same period by sole reason of the fiduciary's diligent service to his employer.

To reach its decision, the Circuit Court has relied upon only the *Restatement of the Law*, an exposition by a collection of authors of what they think the law is or ought to be, a portion of a section from *Fletcher on Corporations*, the opinion of an intermediate California court in *J. C. Peacock, Inc. v. Hasko*, 196 Cal. App. 2d 353, 88 A.L.R. 2d 1430 (1961), and the ruling of a federal court upon the sufficiency of a complaint to withstand a motion to dismiss in *United States v. Bowen*, 290 F.2d 40 (5th Cir., 1961). Such authorities, even if in point, would be of scant significance as the basis for as far-reaching a decision as the Circuit Court has rendered.

In *J. C. Peacock, Inc. v. Hasko, supra*, the employee-officer had, through fraud and chicanery, obtained excessive bonuses from his employer. The corporation successfully sued to recoup the bonuses, but asserted no claim whatsoever to recover salary paid to the defendant. Thus, clearly the holding of the California District Court of Appeals in that case has no relevancy to the issue posed by the facts of this case, wherein there is no claim of fraud or unfaithful service.

In *United States v. Bowen, supra*, the appellate court, without the benefit of an opinion by the district court or a

brief by the appellee, considered on appeal the correctness of the trial court's dismissal of the Government's complaint seeking to recover wages paid to a former employee during the period when he was allegedly engaged actively in arranging to realize, after the impending termination of his employment by the Government, substantial personal profits, at the expense of the Government, from contracts which he arranged with foreign nationals. The court held no more than that a determination of the substantive issues would be dependent upon the particular facts developed during a trial and that a decision upon the merits of the Government's claim should await the presentation of the evidence.

In Fletcher, *Cyclopedia Corporations*, §2145 (Perm. Ed. 1967 Rev. Vol.), the section relied upon by the Circuit Court, the learned author expressly recognizes that, even though an officer of a corporation may have breached his duties, he will not be denied compensation for his labor and beneficial services which have enriched the stockholders. This well-established rule is grounded upon equity and fairness and not upon illogical adherence to inapplicable concepts of imposing a penalty or fine upon an unfaithful servant or agent.

One of the leading cases in support of this rule of fairness in denying forfeiture of compensation is *Richardson v. Blue Grass Mining Co.*, 29 F. Supp. 658 (E.D. Ky., 1939), aff'd. *per curiam* 127 F.2d 291 (6th Cir., 1942), cert. denied 317 U.S. 639, 63 Sup. Ct. 30, 87 L. Ed. 515 (1942). Therein, the managing group of an enterprise had paid its members excessive salaries, had used funds for their personal purposes without paying interest and had deprived other owners of their fair share of the enterprise. Nevertheless, the enterprise had been quite successful financially during a period when similar businesses were suffering economically. The

court, recognizing that there were no inflexible rules applicable in such cases, held that it would be inequitable to deny compensation to the managing group for its efforts, which had substantially enhanced the value of the enterprise. That decision is recognized as embodying the proper test for determining an officer's right to receive or retain compensation for his honest efforts, even though he may have failed to fulfill certain of his duties. *Mardel Securities, Inc. v. Alexandria Gazette Corporation,* 320 F.2d 890 (4th Cir., 1963); Fletcher, *Cyclopedia Corporations,* §2145 n. 71 (Perm. Ed. 1967 Rev. Vol.).

The Circuit Court has, by its decision in this case, ignored the prior holdings of the Courts of Appeals for the Sixth Circuit in the *Richardson* case, *supra,* and the Fourth Circuit in the *Mardel Securities* case, *supra,* and has established in the Tenth Circuit a conflicting rule based upon inflexible application of the ancient concept that unfaithful servants shall have no pay.

The Circuit Court has also disregarded, in passing over the threshold issue, the well-established rules, sometimes referred to as the "Corporate Opportunity Doctrine", which state that, when an opportunity has been rejected by a corporation, a director or officer may thereafter treat the opportunity as his own and the corporation is barred from challenging his action. *Cowell v. McMillin,* 177 Fed. 25 (9th Cir., 1910); *American Investment Co. of Illinois v. Lichtenstein,* 134 F. Supp. 857. (E.D. Mo., 1955); *Little Rock Towel & Linen Supply Co. v. Independent Linen Service Co.,* 237 Ark. 877, 377 S.W.2d 34 (1964); *Lincoln Stores, Inc. v. Grant,* 309 Mass. 417, 34 N.E.2d 704 (1941); 6 Cavitch, *Business Organizations,* § 127.06 (5) (1964).

Consistency in the law and its application is indispensible to the achievement of justice. Consistency and clarity are particularly important in that area of the law defining the obligations, privileges and liabilities of corporate fiduciaries, if American corporate business is to function efficiently. This area of the law is presently receiving widespread attention and study. Notwithstanding this essential requirement for consistency, the Circuit Court has rendered in this case an opinion which conflicts directly with previously-settled principles. If this opinion is not reviewed by this Court, the officers and directors of corporations subject to the jurisdiction of courts within the Tenth Circuit will find themselves burdened with unjustly stringent rules of liability unlike those applied in other circuits. Petitioner respectfully prays, therefore, that a writ of certiorari be issued for review of the judgment of the United States Court of Appeals for the Tenth Circuit.

Respectfully submitted,

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